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IN THE

Supreme Court of the United States

No. 830

Civil

STEVENS BROS. FOUNDATION, INC.,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR RE-HEARING OF ORDER DENYING PETITION FOR WRIT OF CERTIORARI

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Petitioner prays for re-hearing of the order entered April 6, 1964, denying the petition for writ of certiorari in the above-entitled case.

As grounds for this petition, petitioner respectfully represents:

1. Petition for writ of certiorari herein was filed on or about February 13, 1964.

2. Respondent's brief in opposition to said petition was filed with the Court on or about March 20, 1964.

3. Petitioner diligently undertook to cause to be prepared a reply to said brief in opposition.

4. Petitioner had not had an opportunity to file said reply at the time this Court entered its order denying the petition as aforesaid.

5. The reply to said brief in opposition contains matters which properly should be considered by this Court before its determination on whether this Court should issue its writ herein.

6. Copy of the reply brief is attached hereto. Petitioner respectfully requests its examination by the Court and prays that based thereon and upon all the files and proceedings herein the Court issue its writ to the Court of Appeals for the Eighth Circuit.

Respectfully submitted,

JOHN M. SULLIVAN
Attorney for Petitioner

CERTIFICATE

JOHN M. SULLIVAN hereby certifies that the foregoing petition is presented in good faith and not for delay* and further certifies that the petition is presented upon substantial grounds available to petitioner although not previously presented, the substantial grounds being the decision by the Court herein upon the petition for a writ without the Court's consideration of petitioner's reply to the respondent's brief in opposition to the petition.

JOHN M. SULLIVAN

* Delay is not an element in this case inasmuch as before the appeal to the Court of Appeals for the Eighth Circuit, the Foundation paid the entire amount of tax, interest and penalties determined to be owing by the Tax Court, and the effect of the decision by the Circuit Court was to require repayment by the Commissioner of taxes, penalties and interest in an amount in excess of $200,000.00.

IN THE

Supreme Court of the United States

October Term 1963

No. 830

STEVENS BROS. FOUNDATION, INC.,

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COMMISSIONER OF INTERNAL REVENUE,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

Argument

(1) The respondent opposes granting the petition for writ of certiorari and asserts as reasons (a) that maintenance of tax exemption requires an organization be operated "exclusively" for "charitable" purposes, (b) that existence of non-exempt purpose, if substantial in nature, will defeat exemption, (c) that the petitioner aided its founders and consequently it did not thereby operate exclusively for charitable purposes but operated principally, and not, incidentally, for non-exempt purposes (p. 5 et seq.). Such assertions merely repeat the errors committed below.

Among the issues to be considered by this Court is the question whether a participation in an activity negates one purpose and consequently creates another, or whether the participation furthers the principal purpose, as is contended here. This is a basic distinction. By ignoring it respondent merely repeats, without analysis or explanation, the violence done the statutes and the law by equating activity and purpose. The argument set out in the Petition (pp. 10-11) has not been answered, merely ignored.

The respondent enumerates many of the consequences of engaging in the activity described and would have the Court conclude from such enumeration that the activity therefore evidenced an abandonment of one purpose and the adoption of another; that the Foundation's investment in joint construction ventures substituted a new purpose to benefit Foundation's creators for the abandonment of the old "charitable purposes" prescribed in its charter.

The statement (p. 5) "In effect, the taxpayer [Foundation] was being used to finance the construction ventures" is exactly the obverse of the fact. The construction venture was used to fund the Foundation to the extent of $178,387.55 (Pet. A 81).

The allegation that investment in a construction company was "to a substantial extent an effort to benefit its founders" (p. 5) was and is a proposition which no candid presentation of the facts will sanction. It is based upon an assumption (as to which there is no evidence) of benefit in fact, actual or potential, and an inference irreconcilable with all of the evidence of self-serving which is incompatible with the proved charitable purpose and charitable motive.

To sustain the position the respondent must obliterate the distinction between activity and purpose as developed in

Trinidad v. Sagrada Orden de Predicadores, 263 U.S. 578 (1924); and *Samuel Friedland Foundation v. U. S.*, 144 F. Supp. 74 (D.C.N.J. 1956). The respondent consistently perceives purpose in activity. His perception is analogous to his stripping the overalls from a weekend gardener and thereafter forever insisting that it is a dirt farmer in th chauffeur-driven Cadillac on the way to the corporation executive office. This Court is asked to correct such faulty vision.

(2) The respondent's position with respect to the issue of accumulation of income under section 3814 (1) of the 1939 Code (Pet. A-115 - A-116) and section 504 (a) (1) of the 1954 Code (Pet. A-106 - A-107) has undergone an apparent metamorphosis. The implication of the respondent's brief (p. 6) is that the petitioner's goal to accumulate one million dollars to yield sufficient income to carry its current expenses and to leave remaining a substantial sum for charitable purposes is valid, but he contends that such an aim does not have any functional objective, implying presumably that the words of the Foundation's charter which provide that it shall "engage in charitable, educational and public welfare activities of any and all kinds" and "wholly for charity" are not functional objectives. Whether by this distinction he means "charity for the benefit of the Hottentots" is functional, and engagement "in charitable, educational and public welfare activities of any and all kinds" is not, such distinction is a narrow and unwarranted construction of the statutory provisions. The basic exemption statute, section 501 (a) and (c) (3) (Pet. A-104); and the provision, section 504 (Pet. A-106), against accumulations are concerned with "purposes" and not "functional objectives". This Court should review and put aside the arbitrary and capricious constriction of the statute.

Respondent broadly asserts that forcing distributions of current income is explicit in the involved legislative history dealing with that provision. The provision itself plainly states that only unreasonable accumulations are prohibited. Reasonable accumulations are therefore proper. The point here raised is that the determination by the Commissioner, without any standards of any kind, that *this* accumulation for *these* purposes does not suit his whim is arbitrary, capricious and unreasonable.

(3) The respondent contends that retroactive revocation of exemption was justified by Foundation's changed condition which had not been brought to the attention of the Commissioner. This begs the essential question. Pertinent parts of sections 503 (Pet. A-105) and 504 (Pet. A-106) as well as section 502,[1] and corresponding provisions of the 1939 Code (sections 3813, Pet. A-114, 3814, Pet. A-115, and 101[2]) deny exemption under conditions carefully proscribed both as to cause and time when to take effect, particularly under sections 503(a)(2), (d)[3] and 504(a) and 3813(c) and (d)[4]. Such provisions reflect the same principle enunciated in *Automobile Club v. Commissioner*, 353 U.S. 180 (1957), and *Lesavoy Foundation v. Commissioner*, 238 F. 2d 589 (3d Cir. 1956), i.e., withdrawal of exemption without notice is arbitrary and an abuse of discretion. This Court should again confine the Commissioner's discretion to prevent such abuse of authority.

(4) The respondent notes (p. 7) that the petitioner cannot complain about substantial penalties imposed for failure

[1] App. A-1
[2] App. A-1
[3] App. A-2
[4] App. A-3

to file income tax returns since the only reasonable cause was the advice of an attorney that the exemption letter excused the Foundation from filing the returns. The assertion is erroneous and misleading. *The* reasonable cause was and is the proposition that, as a matter of law, the returns were not required to be filed. In addition (Pet. 17-18) the Tax Court applied and the Circuit Court affirmed a construction of the "reasonable-cause" principle which varies from the construction implied by every court except the Tax Court. The proposition that "reasonable cause" is one of fact for the Tax Court posits the application by the Tax Court of the pertinent law.

Respondent would further justify the penalties on the grounds that the petitioner's alleged changed conditions effected a loss of exemption as a consequence of which the petitioner should have known what returns were going to be due. This sort of rationalization evidences the very arbitrary and capricious nature of the Commissioner's position, and fails to note that so long as the exemption letter was outstanding, no returns were due, that petitioner has engaged in a long struggle of, now, ten years, duration to establish that it is an exempt organization, and that the Commissioner moved in, audited and asserted the deficiencies and penalties, here in dispute, even while the petitioner was engaged in efforts to have the exemption issue reconsidered administratively. A review of the entire record will demonstrate the arbitrary and capricious disregard of the existence of, at the very least, the reasonable cause for failure to file returns provided under section 291 (a) of the 1939 Code (Pet. A-113).

(5) Two additional matters should be noted:

(a) The two-page "statement" prejudicially distorts a complicated set of facts and selects therefrom only those

which justify the errors committed by the Tax and Circuit Courts.

(b) Conventionally, the petition and brief in opposition thereto are not the vehicles for a representation of the merits of the cause. Respondent has compressed to three pages of "Argument" his version of two lengthy opinions. Adequate presentation of the merits should be permitted to petitioner by a granting of the writ.

Conclusion

Based upon the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

JOHN M. SULLIVAN

Attorney for Petitioner

APPENDIX

Statutes

1954 INTERNAL REVENUE CODE

Sec. 502. Feeder Organizations

An organization operated for the primary purpose of carrying on a trade or business for profit shall not be exempt under section 501 on the ground that all of its profits are payable to one or more organizations exempt under section 501 from taxation. For purposes of this section, the term "trade or business" shall not include the rental by an organization of its real property (including personal property leased with the real property).

Sec. 503. Requirements for Exemption

* * * * *

(d) FUTURE STATUS OF ORGANIZATIONS DENIED EXEMPTION.—Any organization described in section 501(c)(3) or section 401(a) which is denied exemption under section 501(a) by reason of subsection (a) of this section, with respect to any taxable year following the taxable year in which notice of denial of exemption was received, may, under regulations prescribed by the Secretary or his delegate, file claim for exemption, and if the Secretary or his delegate, pursuant to such regulations, is satisfied that such organization will not knowingly again engage in a prohibited transaction, such organization shall be exempt with respect to taxable years after the year in which such claim is filed.

1939 INTERNAL REVENUE CODE

Sec. 101. Exemptions from Tax on Corporations

* * * * *

An organization operated for the primary purpose of carrying on a trade or business for profit shall not be exempt under any paragraph of this section on the ground that all of its profits are payable to one or more organizations exempt under this section from taxation. For the purposes of this paragraph the term "trade or business" shall not include the rental by an organization of its real property (including personal property leased with the real property).

Sec. 3813. Requirements for Exemption of Certain Organizations under Section 101 (6) and for Deductibility of Contributions made to such Organizations.

* * * * *

(c) DENIAL OF EXEMPTION TO ORGANIZATIONS ENGAGED IN PROHIBITED TRANSACTIONS.—

(1) GENERAL RULE.—No organization subject to the provisions of this section which has engaged in a prohibited transaction after July 1, 1950 shall be exempt from taxation under section 101 (6).

(2) TAXABLE YEARS AFFECTED.—An organization shall be denied exemption from taxation under section 101 (6) by reason of paragraph (1) only for taxable years subsequent to the taxable year during which it is notified by the Secretary that it has engaged in a prohibited transaction, unless such organization entered into such prohibited transaction with the purpose of diverting corpus or income of the organization from its exempt purposes, and such transaction involved a substantial part of the corpus or income of such organization.

(d) FUTURE STATUS OF ORGANIZATION DENIED EXEMPTION.—Any organization denied exemption under section 101 (6) by reason of the provisions of subsection (c), with respect to any taxable year following the taxable year in which notice of denial of exemption was received, may, under regulations prescribed by the Secretary, file claim for exemption, and if the Secretary, pursuant to such regulations, is satisfied that such organization will not knowingly again engage in a prohibited transaction, such organization shall be exempt with respect to taxable years subsequent to the year in which such claim is filed.

* * * * * *